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96TH CONGRESS } SENATE { REPORT
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EXPORT TRADING COMPANIES, TRADE ASSOCIATIONS, AND TRADE SERVICES

REPORT

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

TO ACCOMPANY

S. 2718

together with

ADDITIONAL VIEWS

MAY 15 (legislative day, JANUARY 3), 1980.—Ordered to be printed

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EXPORT TRADING COMPANIES, TRADE ASSOCIATIONS, AND TRADE SERVICES

MAY 15 (legislative day, JANUARY 3, 1980).—Ordered to be printed

Mr. STEVENSON (for himself and Messrs. HEINZ, BENTSEN, ROTH, GLENN, SCHMITT, MELCHER, TSONGAS, LUGAR, STEWART, and JAVITS), from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany S. 2718]

The Committee on Banking, Housing, and Urban Affairs, to which was referred the bill (S. 2718) to encourage exports by facilitating the formation and operation of export trading companies, export trade associations, and the expansion of export trade services generally, having considered the same, reports favorably thereon and recommends that the bill do pass.

HISTORY OF THE LEGISLATION

The concept of legislation to encourage the formation of U.S. trading companies was discussed at hearings on U.S. export policy held in early 1978 by the Subcommittee on International Finance (see, in particular, parts 3, 6, 7, and 8 of those hearings). The Subcommittee's report on the need for a U.S. export policy, issued in March 1979, included a recommendation that U.S. export trading companies be established to expand exports of the products of smaller U.S. producers and that the Webb-Pomerene Act be revised to clarify antitrust treatment of export activity.

S. 1663, the Export Trading Company Act of 1979, was introduced by Senator Stevenson on August 2, 1979, and referred jointly to the Committees on Banking, Housing, and Urban Affairs and Finance. Hearings were held on the bill before the Subcommittee on International Finance on September 17 and 18, 1979. Also considered during the hearings were three bills to amend the Webb-Pomerene Export Trade Act of 1918 concerning export trade associations: S. 864, the

Export Trade Association Act of 1979, introduced by Senators Danforth, Bentsen, Chafee, Javits and Mathias on April 4, 1979; S. 1499, the Export Trade Activities Act, introduced by Senator Roth on July 12, 1979; and S. 1744, introduced on September 13, 1979, by Senator Stevenson for Senator Inouye.

The Subcommittee received testimony from Luther H. Hodges, Jr., Under Secretary of Commerce; C. Fred Bergsten, Assistant Secretary of the Treasury for International Affairs; Ky P. Ewing, Deputy Assistant Attorney General in the Antitrust Division of the Justice Department; Daniel Schwartz, Deputy Director of the Bureau of Competition of the Federal Trade Commission; Senators Danforth, Bentsen, Chafee, Mathias and Javits; and a number of other witnesses. The testimony ranged across all the issues raised in the bills: antitrust treatment of trade associations and trading companies, tax treatment of export trading companies, Federal assistance for start-up costs and financial leverage of export trading companies, and bank ownership of export trading companies.

A new bill, S. 2379, the Export Trading Company Act of 1980, was introduced on March 4, 1980, by Senators Stevenson, Heinz, Javits, Bentsen and Glenn. The bill contained revised versions of each of the basic provisions of S. 1663. On February 26, 1980, Senators Danforth, Bentsen, Chafee, Mathias and Javits introduced a revised version of their legislation to reform the Webb-Pomerene Act: Amendment 1674 to S. 864.

Hearings were held on the revised legislative proposals on March 17 and 18, and April 3, 1980. Testimony was received from Secretary of Commerce Philip Klutznick, speaking on behalf of the Administration and accompanied by Assistant Secretary of the Treasury C. Fred Bergsten, Deputy U.S. Trade Representative Robert Hormats, and Assistant Secretary of State for Economic Affairs Deane Hinton; Deputy Assistant Secretary of State Erland Heginbotham (who appeared in his individual capacity as an expert on Asian trade); Governor Henry Wallich of the Board of Governors of the Federal Reserve System, (who was unable to appear in person due to foreign travel commitments): W. Paul Cooper, President of Acme-Cleveland Corporation and representing the National Machine Tool Builders Association; J. D. Minutilli, President of Commercial Credit Company; Ted D. Taubeneck, President of Rockwell International Trading Company and representing the Chamber of Commerce of the United States; E. Anthony Newton, Senior Vice President of Philadelphia National Bank; James B. Sommers, President, the Bankers Association for Foreign Trade and Executive Vice President of North Carolina National Bank; Lawrence A. Fox, Vice President of the National Association of Manufacturers; Jerry L. Hester, President of International Trade Operations, Inc.; Robert L. McNeill, Executive Vice Chairman of the Emergency Committee for American Trade; John R. Liebman, General Counsel of the Export Managers Association of California, Inc.; Ruth Schueler, President of Schueler and Company, Inc., representing the Subcommittee on Export Promotion of the President's Export Council; and Thomas M. Rees, representing the Task Force on International Trade of the White House Conference on Small Business.

The full Committee marked up a Committee print on May 12, 1980, which contained revised versions of S. 2379 and Amendment 1674 to S. 864, and agreed to report favorably an original Committee bill.

Purpose of the Legislation

The purpose of the legislation is to improve U.S. export performance by facilitating the creation of U.S. export trading companies which could perform export services for tens of thousands of small and medium-sized American producers. Despite the success of trading companies as "export middlemen" for European, Japanese, and Korean producers, such companies have been slow to develop in the U.S. due to deterrents presented by banking regulations, antitrust uncertainties, and the traditional insularity of the U.S. market. This legislation modifies provisions of existing law which have acted to discourage the establishment or expansion of export trading companies, and offers modest incentives to the development of such companies.

The bill would provide for certification of antitrust exemption for specified export trade activities of such companies and of export trade associations; afford tax and financing incentives to encourage formation and growth of export trading companies, including existing export management companies; direct the Export-Import Bank to develop an improved guarantee program to support commercial loans to U.S. exporters; require the Secretary of Commerce to provide information to U.S. producers regarding export trading companies and other firms offering export trade services; and permit banks and banking institutions to make limited investments in export trading companies. The legislation is intended to lay the basis for a significant expansion of export services and, thereby, U.S. exports.

Need for the Legislation

This legislation is necessary to encourage the formation of export trading companies and export trade associations designed to link potential U.S. exporters with overseas markets. The Department of Commerce and others have estimated up to 20,000 U.S. manufacturers and agricultural producers offer goods and services which could be highly competitive abroad. Yet the small size and inexperience of these firms leave them ill-equipped to absorb the front-end costs and risks involved in developing overseas markets.

Greater efforts to encourage and assist U.S. producers to export directly are desirable, but for most producers the marginal costs of developing fully their export opportunities abroad will prove prohibitive. Export expansion on the scale required to offset U.S. trade deficits will depend on the development of intermediaries, including export trading companies, which, by diversifying trade risk and developing economies of scale in marketing, financing, and other export trade services, can do the exporting for large numbers of U.S. producers.

Although a variety of existing enterprises do provide export services to U.S. producers—freight forwarders, brokers, shippers, insurance companies, comercial banks, export management companies, advertising firms, trade lawyers, foreign purchasing agents, and others—most fulfill only one or a few of the many functions required to engage in export trade. In constrast, most European countries, as well as Japan and Korea, possess sophisticated, large-scale general purpose trading companies which perform the full range of requisite functions for potential exporters; the success of such companies has contributed significantly to the export earnings of all of our major trade competitors.

Despite the similar success of foreign-owned export trading companies operating in the U.S. over the past few years, the growth of U.S.-owned export trading companies has been slow, except in a few sectors such as grain and raw materials trade.

If U.S. export trading companies are a sound business proposition, why have not the working of the marketplace and American enterpreneurship produced such companies already? First, the U.S. domestic market has been much larger and more prosperous than foreign markets—until recently. Belatedly U.S. companies are beginning to see the greater growth possibilities in foreign markets, but foreign producers are already well organized for exporting and can offer quality products at competitive prices. Second, many foreign markets have been largely closed to U.S. exporters. China is an extreme example, but Japan and other countries have maintained high tariff walls and nontrariff barriers to imports almost as effective as the isolation of China. Due to the recently concluded Multilateral Trade Agreements in GATT and persistent U.S. bilateral efforts, trade barriers are being reduced. Foreign competitors, however, with a longer history of aggressive exporting, are better poised to seize these new market opportunities; U.S. negotiating successes may only be opening markets for our competitors. Finally, U.S. laws and regulations, as well as traditional business and banking practices, have discouraged cooperative export trading companies, export trade associations, or bank participation in export trade activity.

Legislation is needed to remove these deterrents and to encourage the formation and growth of general purpose export trading companies by means of tax and financing incentives. Rapid formation of export trading companies on a scale sufficient to affect overall U.S. export levels will require the involvement of banks and major corporations, whose financial resources, international marketing networks and trade financing experience position them well to play a major role in the establishment of export trading companies. This legislation is needed to enable banks and banking institutions to make limited investments in export trading companies, subject to prior approval and conditions imposed by Federal bank regulatory agencies for all controlling investments.

The bill also provides for revision of the Webb-Pomerene Act of 1918 to clarify the antitrust provisions applicable to export trade associations and to provide a certification procedure enabling export trading companies and other such associations to receive antitrust clearance for specified export trade activities. The lack of clear cut antitrust immunity provided exporters by the 1918 legislation and the exclusion of services from its coverage has severely limited the statute's effect on exports. Under the review procedures established by the present legislation any U.S. company may determine in advance exactly which export trade activities would be immune from antitrust suit and organize its operations accordingly.

In order to encourage the direct involvement of smaller exporters in the formation of export trading companies, the legislation urges the Economic Development Administration and the Small Business Administration to give special attention to the financng needs of small and medium-sized concerns interested in exploring export opportunities in this manner. It authorizes an additional $20 million per year in fiscal years 1981 through 1985 to EDA and SBA to support loans or guarantees for these purposes.

This legislation would also improve the financial leverage of export trading companies. It directs the EXIM Bank to establish an expanded guarantee program for commercial credits secured by export accounts receivable or inventory held for exportation, if the Board of Directors of the Bank determines the private credit market is inadequate and EXIM guarantees would facilitate exports which would not otherwise occur.

The bill would direct the Secretary of Commerce to promote actively the formation of export trading companies and the dissemination of information about related export opportunities.

Finally, the legislation would extend the tax deferral available under the DISC (Domestic International Sales Corporation) provisions of the tax code to all export trading company income, derived from exports handled or the provision of trade services. The use of subpart S of the tax code, permitting certain passthroughs to shareholders of closely held corporations, would be allowed for some export trading companies. The Department of Commerce, with the assistance of the International Revenue Service, is directed to prepare a guide to help export trading companies form DISCs or elect subpart S tax treatment.

These provisions would remove the most serious deterrents to the emergence of significant U.S. export trading companies. The legislation would foster competition by decreasing government regulation, and would offer the potential for greatly increased U.S. export competitiveness with minimal direct Federal government participation.

Explanation of the Bill

TITLE I—EXPORT TRADING COMPANIES

1. Definitions

The bill defines an export trading company as a U.S. company "organized and operated principally for the purposes of: (A) exporting goods or services produced in the United States; and (B) facilitating the exportation of goods and services produced in the United States by unaffiliated persons by providing one or more export trade services." The definition is intended to encompass most existing firms which offer export trade services to U.S. producers to whom they are not affiliated, while doing some exporting at their own risk. Many of these American firms, called export management companies or trading companies, are very small and have difficulty obtaining adequate financing to expand their operations. Encouragement and assistance to such firms are major objectives of the legislation.

The definition of an export trading company is meant to exclude firms by any name which export solely the goods or services of the company itself, its parent company or its subsidiaries, or other members of the corporate family. Many major American corporations have subsidiaries which may be called trading companies, but which in fact export only the products of the corporate group. If such companies wish to qualify as export trading companies as defined in the bill, they will need to do some exporting for, or provide trade services to, unaffiliated persons (generally, small and medium size U.S. firms). The bill does not establish minimum percentages for the proportion of export activity an export trading company must perform on behalf of unaffiliated persons; instead, the Federal agencies with administrative responsibilities related to the provisions of the bill are given flexibility to interpret and apply the definitions as seems most appropriate to further the purpose of the Act.

Because another principal objective of the Act is to induce major corporations with extensive export trade experience to offer exporting services to less experienced U.S. producers, it would be consistent with the Act to expect export trading companies to develop a significant portion of their total business in the export of goods or services produced by unaffiliated persons, or in the provision of export trade services to such persons. For example, a company claiming to be organized and operated principally as an export trading company within the definition in section 103(5) of the Act, but which over a reasonable period of years received on the average less than 10 percent of its gross sales or income through exporting goods for, or providing export services to, unaffiliated U.S. persons might be disqualified.

The bill also defines U.S. exports and establishes a presumption that the principal business of a U.S. export trading company should be U.S. exports. Export trade is defined to mean exports of goods produced in the United States or services provided by U.S. citizens or otherwise attributable to the United States. The bill requires that at least 50 percent of the value of such goods or services must be of U.S. origin in order for the goods and services to be considered U.S. exports for purposes of the Act. Fifty percent was chosen because it is the existing standard in the Internal Revenue Code for eligible "export receipts" of Domestic International Sales Corporations (DISCs). Setting a higher minimum threshold for U.S. content would not only create the legal anomaly that a sale could be an "export" for DISC purposes but not for meeting the definition of an export trading company, but could also unreasonably restrict the trade possibilities for companies seeking to qualify as export trading companies.

Section 103(5) defines an export trading company as one engaged "principally" in export trade, both on its own behalf and on behalf of unaffiliated persons. Thus, the presumption is established that on the average at least one-half the company's total business—which may include some domestic trade, some import trade and some "third-party" international trade wholly outside U.S. commerce—will be directly related to U.S. exports which must contain at least 50 percent value attributable to the U.S. If the company exports a product with 49 percent of the value added in the U.S., for example, the export sale counts as part of the "other" business of the company, not as part of its export business. Furthermore, successful trading companies must develop two- and three-way trade in order to reduce foreign exchange risk and maintain good relations with foreign customers. The presumption established in the Act will not be an easy one for trading companies to meet, but it does insure that "export trading companies" as defined in the Act will be principally and substantially engaged in exports of goods and services produced primarily by Americans.

The term "export trade services" is defined in section 103(4) of the Act to include a broad range of services provided in order to facilitate the export of goods or services produced in the United States. While the Act's purpose is to enable the performance by export trading companies of a wide range of services to expand U.S. exports, including transportation and forwarding, the bill is not intended to repeal or amend the provisions of the Shipping Act of 1916 (46 U.S.C. 800 et seq.), which govern the licensing of independent ocean freight forwarders. Export trading companies wishing to render forwarding services may do so upon qualifying for, and receiving, a license under that Act.

2. Promotion by Secretary of Commerce

The bill directs the Secretary of Commerce to promote and encourage the formation and operation of export trading companies by providing information and advice to interested persons and by facilitating contact between producers of exportable goods and services and firms offering export trade services. The provision is intended to lead to a better two-way referral system by the Department of Commerce. The Department has an established role in assisting companies interested in learning how to export and in acquiring foreign market information, but in many cases a more effective approach may be to put companies in contact with export trading companies or other private enterprises which can either provide export assistance or do the actual exporting. Conversely, as part of the Department's responsibility to promote export trading companies, it should help such companies and others providing export trade services to locate and contact U.S. producers of exportable goods and services. It is the Committee's view that the Commerce Department should be more responsive than it has been in the past to the needs of export management companies and international trade consultants to make contact with potential clients.

3. Ownership by Banks

This legislation seeks to stimulate a form of business activity in the United States which has been neglected by major corporations and investors and has consequently been deprived of significant financial resources, as the history of U.S. export management companies clearly demonstrates. In an economy which has been primarily oriented to the domestic market, it is not obvious where the investment and entreneurship can be found to establish export trading companies on an economical scale, and one which can also make a difference in the U.S. trade accounts. This legislation attempts to stimulate initiative from at least three possible sources: (1) accelerated internal growth by existing U.S. export management or export trading companies; (2) formation of independent export trading companies fostered by major corporations with international trade experience; and (3) investments by U.S. banking institutions in new or existing export trading companies.

Banks with international offices, experience in trade financing, business contacts abroad, international marketing knowledge, and familiarity with domestic U.S. producers are the most likely source of leadership in forming export trading companies. Their skills which are important to the organization and management of trading companies. A number of large non-Japanese trading companies are owned by banks in Europe. For example, Hongkong and Shanghai Banking Corp. owns a 33 percent controlling interest in Hutchinson Whampoa

Limited; Midland Bank Limited owns controlling interests in at least three trading companies; Barclay's Bank International owns 24.5 percent of Tozer, Kernsley and Millbourn; Credit Lyonnais owns 80 percent of Essor PME; and Banco de Brazil owns 100 percent of Beke Company.

The potential contribution of U.S. banks was explained by Erland Heginbotham, Deputy Assistant Secretary of State for East Asian and Pacific Affairs in testimony on March 18, 1980, before the International Finance Subcommittee: "The development of bank-owned trading companies promises to offer enormous potential for overcoming most of the major disadvantages now seriously inhibiting U.S. exports to Asia. A number of European banks now operate some of the largest European-owned trading companies . . . Banks bring not only assets but almost all of the supporting facilities and services which U.S. exporters now most lack by contrast with competitors. More importantly, banks can encourage and help exporters develop a longer-term view of, and presence in the market. Bank-affiliated trading companies would have special effect on encouraging more medium and small exporters who are now discouraged by the remoteness and strangeness of foreign markets and buyers, exchange risks, and by the complexity and expense of documentation."

Section 105 of the bill would permit U.S. banks to make limited investments in export trading ocmpanies, subject (except for non-controlling investments of less than $10 million) to the prior approval of Federal bank regulatory agencies, and subject to conditions and safeguards designed to ensure the safety and soundness of the banks and prevent favoritism in bank lending to a trading company in which it has an interest on the company's customers.

U.S. banks have been excluded from most commercial activities, including direct participation in export trade for more than a century. Among the reasons given for maintaining the traditional distinctions are: (1) that banks should focus on loans and deposits and can better exercise independent judgment on whether or not to make a loan if they are prohibited from holding a stake in the management of actual or potential borrowers; (2) that banks could be exposed to unfamiliar and excessive risks in commercial trading and the holding of inventories; (3) that the bank regulatory agencies lack the capacity to evaluate the commercial risks banks would encounter in owning export trading companies; (4) that bank capital is low and should be reserved for support of bank loans; and (5) that bank-owned export trading companies or companies dealing with them may have preferential access to bank credit.

A majority of the Committee members, while supporting the general principle of separation of banking and commerce, believes there is good and sufficient reason to make an exception on a controlled basis for limited and conditional bank ownership of export trading companies in order to strengthen the Nation's capacity to meet non-traditional international trade competition. The majority of the Committee members further believe that the bill as ordered reported contains prohibitions, restrictions, limitations, conditions and requirements more than ample to meet each of the concerns raised with respect to bank ownership of export trading companies:

(1) The bill prohibits banks from making loans to any export trading company in which the bank holds any interest whatsoever, and to

any customers of such company, "on terms more favorable than those afforded similar borrowers in similar circumstances" or involving "more than the normal risk of repayment" or presenting "other unfavorable features". Thus, banks would be barred from making preferential or unusually risky loans to export trading companies or their customers.

(2) The bill prohibits banking organizations from owning any interest in any export trading company which "takes positions in commodities or commodities contracts other than as may be necessary in the course of its business operations." That is, speculation in commodities is forbidden for any trading company controlled by a banking organization.

(3) The bill empowers the Federal financial institutions regulatory agencies (the Federal Reserve Board, the Comproller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board for Federal savings banks) when acting on a bank's application to take to take a controlling interest in an export trading company, to impose any conditions they deem necessary

> (A) to limit a banking organization's financial exposure to an export trading company, or (B) to prevent possible conflicts of interest or unsafe or unsound banking practices.

(4) The bill directs the Federal financial institutions regulatory agencies to establish standards with respect to the taking of title to goods by any export trading company subsidiary of a banking organization, standards "designed to ensure against any unsafe or unsound practices that could adversely affect a controlling banking organization investor, including specifically practices pertaining to an export trading company subsidiary's holding of title to inventory." Any changes in the trading company's practices with respect to taking title would have to be approved in advance by the Federal agency.

(5) The bill would bar any banking organization from taking a controlling interest or making any investment over $10 million in any export trading company without receiving the prior approval of the appropriate Federal financial institutions regulatory agency. The Federal agency would be required to disapprove any application for which it finds

> That the export benefits of such proposal are outweighed in the public interest by any adverse financial, managerial, competitive, or other banking factors associated with the particular investment.

(6) The bill would prohibit aggregate investments by any banking organization of more than 5 percent of its consolidated capital and surplus in one or more export trading companies.

(7) The bill would prohibit the total of a banking organization's historical direct and indirect investments in a trading company and loans to such company and its subsidiaries from exceeding 10 percent of the bank's capital and surplus.

(8) The bill would allow the appropriate Federal agency

> Whenever it has reasonable cause to believe that the ownership or control of any investment in an export trading company constitutes a serious risk to the financial safety, soundness, or stability of the banking organization and is incon-

> sistent with sound banking principles or with the purposes of this Act or with the Financial Institutions Supervisory Act of 1966, order the banking organization . . . to terminate . . . its investment in the export trading company.

The majority of the Committee are supported in their view that the bill contains appropriate Federal regulatory authority over bank investments in export trading companies by the Administration, by the Comptroller of the Currency, and (with one exception) by the Federal Reserve Board. For the views of the agencies, see the letters in the Appendixes to this report. The sole exception is the Board's view that Federal bank regulatory agencies should not be authorized to approve any controlling investments by banks in export trading companies. Specifically, the Board would prohibit any one banking organization from acquiring more than 20 percent of export trading companies and any group of banking organizations from acquiring more than 50 percent of a trading company. The Board would accept non-controlling investments, subject to the provisions contained in the bill. The Board appears to question the ability, as well as the propriety, of permitting banks, either singly or as a group to manage export trading companies.

The Bankers' Association for Foreign Trade, in testimony before the Subcommittee on International Finance on March 18, 1980, stressed the importance of flexibility with respect to the types of permissible bank investments in export trading companies:

> Because the trading company concept is new to the United States, it is difficult for me to indicate at this time the precise ways banking organizations may choose to participate. Some banking organizations may want to finance export trading companies and their customers but not take an equity position; others are more interested in investing in export trade service firms than export trading companies; and others are interested in investing in export trading companies, but may differ on the scope of participation they may find appropriate *e.g.*, some are interested in joint ventures and others are interested in forming their own subsidiaries. Given this diversity of interest, we support S. 2379's flexible approach and would thus recommend against foreclosing any options at the present time because trading companies must and will evolve in response to market forces, and banking organization involvement will be controlled through the existing bank regulatory framework.

James B. Sommers, Executive Vice President of North Carolina National Bank, testified that banks might wish to organize export trading companies to put together large "turnkey" export projects, e.g., the construction of a plant in a developing country. Such companies will most likely be regional trading companies involving more than one banking organization. E. Anthony Newton, Senior Vice President of Philadelphia National Bank, testified that his bank has an overseas financing subsidiary which could be a more effective competitor in the Far East if it could take title to goods—an activity it safely engaged in before acquisition by Philadelphia National Bank. The Federal Reserve Board would have the Congress deny it the authority to approve such investments and activities by U.S. banks. For example, even a trading company organized by banking organizations for a single project overseas would be prohibited.

Permitting banking organizations to take controlling interests in trading companies promotes the safety and soundness of the investing banking organization, since it gives them greater ability to protect their investment through control of the business operations of an export trading company. A banking organization is more likely to become involved in an export trading company if it has a substantial or controlling voice in management. Arbitrary statutory limits on controlling investments serve only to lock banking organizations out of a management roll; increase the risks of their investment, and deny to trading companies their substantial international expertise. The regulatory controls included in the bill insure that the greater degree of bank control, the greater degree of bank regulatory agency control. The Committee believes this flexible approach adopted in the bill is necessary to encourage effective bank participation. Without initiatives by U.S. banks, the effort to stimulate U.S. export trading companies would be seriously weakened.

The amounts of bank capital potentially involved and the risks to the banks must be put into perspective based on the restrictions in the bill. Total capital of all the banks in the United States is about $98 billion. Because the bill limits aggregate investments to 5 percent of capital, if every bank in the country from the smallest to the largest were allowed by the Federal regulators to invest the maximum amount under the Act, the total investment allowed would be $4.9 billion. Because the bill limits the total of investments and loans in export trading companies to 10 percent of capital, if every bank in the country both invested and lent the maximum under the Act, the total of all investments and loans would be $9.8 billion. Realistically, only a small fraction of U.S. banks, large and small, will invest in, or lend to, an export trading company.

Both the banks and the Federal bank regulatory agencies can be expected to proceed cautiously. At most, $1 billion in total bank investments and loans to export trading companies might be anticipated within 5 years after enactment. In an economy which has long passed the $1 trillion mark, such amounts seem unlikely to dry up credit or significantly affect bank capital. Investments in export trading companies should strengthen bank capital by earning profits and diversifying risks. The 10 percent limit on combined investments and loan is quite conservative, considering that state banks in several states, including New York, may lend up to 25 percent of capital to a single borrower, and that some banks have more than half of their capital exposed in loans to borrowers in a single developing country.

In considering individual applications or notifications, the appropriate Federal agency may determine that safeguards are needed to protect against certain activities or practices which could reflect adversely on the banking organization investor. For example, the agencies may want to prohibit an ETC owned by a banking organization from engaging in manufacturing operations or owning other commercial concerns. They may also want to set conditions designed to insure that a bank-owned ETC is run in a financially-sound manner in order to safeguard the reputation and integrity of the banking organization investor.

Conditions appropriate to an ETC wholly-owned or controlled by a banking organization may be wholly inappropriate where a banking organization is to be a non-controlling investor. The size of the banking organization and ETC, the degree of banking organization involvement, and the size and financial strength of other participants are all factors that need to be weighed. Conditions imposed by the Federal banking agencies should not unnecessarily disadvantage, restrict or limit bank-owned ETCs in competing in world markets or achieving the purposes of section 102 of the Act. Conditions thus should be carefully drawn to meet legitimate concerns, without unduly handicapping bank-owned ETCs in meeting foreign competition. The Committee strongly believes that such conditions should not serve to discourage involvement of banking organizations, but rather should encourage their participation in the most prudent manner.

4. Initial Investments and Operating Expenses

The bill provides in section 106 for greater support by the Economic Development Administration (EDA) and the Small Business Administration (SBA) for the formation and expansion of export trading companies. Both agencies have given some support to export-related activities in the recent past, but only in minimal amounts. The Assistant Secretary of Commerce for Trade Development, Herta Lande Seidman, testified before the International Finance Subcommittee on April 28, 1980:

> Through the facilities of the Economic Development Administration, the Commerce Department is in a position to make loans and grants to meet the combined objectives of job creation and export promotion. In 1979, for example, EDA funding of export-related efforts amounted to $6.7 million in loans and $2.5 million in grants. These funds supported, among other efforts, an extensive textile, apparel, and footwear export expansion drive and promotion projects of the New York/New Jersey Port Authority. We in the International Trade Administration are working closely with EDA to develop grant- and loan-making procedures to ensure that the export programs funded by EDA are closely meshed with Trade Development activities in ITA. EDA is prepared in 1980 to supply a somewhat larger amount in grants and a significantly larger amount in loans for trade facilitation programs through its trade adjustment assistance, distressed area and other programs. Similar levels of activity are feasible in the future if funding for those programs continues. EDA, depending on its resources, is interested in giving continuing support to export-related programs.

The Small Business Administration, according to President Carter's Export Policy statement of September 26, 1978 was to provide up to $100 million in assistance to small businesses getting started in exporting. Less than $5 million has actually been used by SBA for this purpose, and SBA is widely charged with lack of interest and expertise in export development.

S. 2379 would have provided a $100 million, five-year facility in the Export-Import Bank to assist the formation of export trading companies by providing loans on a matching basis of not more than $1 million per year or $2.5 million in total to applicants to assist with initial investments and operating expenses associated with launching an export trading company. The assistance would only have been available where private credit was inadequate and other criteria were met. Because the Export-Import Bank and the Administration opposed lodging the program in the Bank, the present legislation vests responsibility in EDA and SBA to help export trading companies meet start-up costs.

Section 106(a) would direct EDA and SBA, when considering loan or guarantee applications from export trading companies, to give "special weight to export-related benefits, including opening new markets for United States goods and services abroad and encouraging the involvement of small or medium-size businesses or agricultural concerns in the export market." The purpose of the amendment is to encourage EDA and SBA to consider favorably those applications with export benefits which also meet other criteria which EDA and SBA are required to consider. The provision is not intended to override or dilute other considerations the agencies are required to take into account.

Section 106(b) would authorize appropriation of an additional $20 million per year in fiscal years 1981 through 1985 to either EDA or SBA to support loans (or guarantees, if necessary) provided to meet the purposes of section 106(a). If existing authorizations and appropriations thereunder are deemed adequate by the Appropriations Committees of the Congress to meet the purposes of section 106(a), the authority of section 106(b) would not be used.

5. Guarantees by Export-Import Bank

Section 107 authorizes and directs Eximbank to establish a guarantee program for commercial loans to U.S. exporters secured by export accounts receivable or inventories of exportable goods, when in the judgment of the Board of Directors:

1. Private credit is inadequate to enable otherwise credit-worthy exporters to complete export transactions, and
2. Such guarantees would facilitate exports which would not otherwise occur.

The Administration did not object to guarantees in support of loans against export accounts receivable, but contended that inventories are adequately financed by the private sector. The amendment takes the Administration's view into account by permitting the guarantee program to operate only to the extent that the Board of Directors determines the private credit market is not providing adequate financing. It is the intent of the Committee that the guarantees be directed primarily toward securing credit for small exporters. The amounts of guarantees would be limited by limits set in annual appropriations Acts.

TITLE II—EXPORT TRADE ASSOCIATIONS

Under the Export Trade Act of 1918, commonly known as the Webb-Pomerene Act (15 U.S.C. 61–65), the joint exporting activities of export trade associations (associations engaged solely in export trade) receive a limited exemption from the Sherman and Clayton Antitrust Acts.

The Webb-Pomerene Act was an outgrowth of a report on foreign trade activities affecting U.S. companies prepared by the Federal Trade Commission in 1916. The Commission's report found that American manufacturers and producers were disadvantaged in attempting to enter foreign markets individually because of strong combinations of foreign competitors and organized buyers. The report concluded that in order for small American producers and manufacturers to enter world markets on a profitable basis and on more equal terms with these foreign combinations, they should be permitted to cooperate in their exporting efforts without fear of prosecution under the antitrust laws.

Section 2 of the Webb Act exempts from the Sherman Act (which prohibits contracts, combinations, or conspiracies in restraint of trade occurring either in interstate commerce or in commerce with foreign nations) an association entered into for the sole purpose of engaging in export trade as long as the association, its acts, or any agreements into which the association enters do not: (1) restrain trade within the United States; (2) restrain the export trade of any domestic competitor of the association; or (3) artificially or intentionally influence prices within the United States of commodities of the class exported by the association. The Act also provides for oversight of Webb-Pomerene associations by the Federal Trade Commission.

Between 1930 and 1935 Webb-Pomerene associations numbered 57 and accounted for approximately 19 percent of total U.S. exports. By 1979 the number of associations had dwindled to 33 and their share of total U.S. exports had dipped to less than 2 percent.

The reasons for this poor showing are many. First, the vast majority of the 250 or so Webb-Pomerene associations formed over the last 60 years lacked sufficient product-market domination to exert foreign market price control and membership discipline. Second, the business community traditionally has placed top priority on tapping the vast domestic market and has been much slower to focus on the prospects overseas. Third, the ever expanding U.S. service industries have been excluded from qualifying for the Act's antitrust exemption, while cooperative and joint ventures have become increasingly important in the exportation of services. Fourth, and perhaps most important, the Department of Justice, and to a lesser extent the Federal Trade Commission, have been perceived by the business community as exhibiting a thinly veiled hostility toward Webb-Pomerene associations. The vagueness of the Webb-Pomerene Act leaves uncertain what activities will constitute a substantial restraint of domestic trade. As a result, the threat of antitrust litigation has served as a deterrent to broader utilization of the Webb-Pomerene Act.

With the increasing emphasis on the need to improve the competitiveness of U.S. companies in the world marketplace has come an awareness of the need to reduce the domestic barriers to exports. The provisions of this bill are intended as a step toward that goal. At the same time, however, the bill contains numerous procedural and substantive safeguards to ensure that this goal is not achieved at the cost of violating traditional principles of U.S. antitrust law.

6. Antitrust Exemption for Certified Export Trade Activities

Title II does the following: First. It makes the provisions of the Webb-Pomerene Act explicitly applicable to the exportation of services (the National Commission for the Review of Antitrust Laws and

Procedures made this same recommendation in its report to the President in January 1979);

Second. It expands and clarifies the Act's antitrust exemption for export trade associations and export trading companies;

Third. It requires that the antitrust immunity be made contingent upon a certification procedure and in conformance with existing standards of antitrust law;

Fourth. It transfers the administration of the Act from the Federal Trade Commission to the Department of Commerce;

Fifth. It provides for procedures whereby the Justice Department and the Federal Trade Commission can provide their advice to the Department of Commerce during the certification process, and can seek invalidation of any certification which fails to conform to the substantive standards of the Act;

Sixth. It creates within the Department of Commerce an office to promote the formation of export trade associations and export trading companies; and

Seventh. It provides for the establishment of a task force whose purpose will be to evaluate the effectiveness of the Webb-Pomerene Act in increasing U.S. exports and to make recommendations regarding its future to the President.

Title II reflects a recognition of the significant contribution to the promotion of U.S. export trade which can be made by export trade associations and export trading companies if they are allowed to engage in specific joint activities without fear of prosecution under the antitrust laws. Title II provides immunity from the application of U.S. antitrust laws for specified export trade, export trade activities and methods of operation of export trade associations and export trading companies only when: 1) the proposed export activities are determined not to be in violation of specified antitrust standards; 2) there is an established need for the immunity; and 3) the association or company successfully completes the certification process required in the bill.

7. Certification procedures

The certification process mandates that the Department of Commerce, after consulting with the Justice Department and the Federal Trade Commission, determine that the export trade activities of the association or company violate none of the substantive standards of antitrust law set forth in Section 204(a) of the bill. That Section, which amends the second and fourth sections of the Webb-Pomerene Act (15 U.S.C. 62 and 64), sets out eligibility criteria for the antitrust exemption afforded under the Act for export trade associations and trading companies.

With the exception of the requirements in paragraphs (1) and (6) of Section 204—provisions that impose further criteria for eligibility in addition to those found in the standards of the current Webb-Pomerene Act—the substantive law of antitrust as modified by the Webb-Pomerene Act has not been altered. As the court stated in *United States* v. *Minnesota Mining and Manufacturing Company*, 92 F. Supp. 947 at 965 (D. Mass. 1950):

> Now it may very well be that every successful export company does inevitably affect adversely the foreign commerce of those not in the joint enterprise and does bring the

> members of the enterprise so closely together as to affect adversely the members' competition in domestic commerce. Thus every export company may be a restraint. But if there are only these inevitably consequences an export association is not an unlawful restraint. The Webb-Pomerene Act is an expression of Congressional will that such a restraint shall be permitted.

The amendment of the Webb-Pomerene Act by Section 204(a) of Title II, with the exceptions as noted above, is a codification of court interpretations of the Webb-Pomerene exemption to domestic antitrust law. Further, the amendment is consistent with the enforcement policy of the Department of Justice. As stated by Ky Ewing, Deputy Assistant Attorney General, Antitrust Division, Justice Department, during hearings on S. 864 (now Title II) before the International Finance Subcommittee:

> We note (that S. 864) would require that a restraint of U.S. domestic trade be substantial before the exemption would disappear. The purpose of this proposal . . . is to bring the act into what we conceive to be the current state of antitrust law interpreted by the court. (September 17, 18th hearing record on Export Trading and Trade Associations, p. 138)

Similarly, Daniel Schwartz, Deputy Director, Bureau of Competition, Federal Trade Commission, testified that the antitrust standards specified in S. 864 "are essentially equivalent to the standards of the Webb-Pomerene Act." (Id. at p. 194).

In his prepared statement, Mr. Ewing further explained that:

> The judicially accepted legal threshold test for applicability of the Sherman Act to activity abroad places a heavier burden on government and private plaintiffs than that applicable domestically. The presence of a substantial and foreseeable effect on U.S. domestic or foreign commerce is required, not merely some minimal effect. (Id. at 144).

Mr. Ewing also noted in his testimony before the Subcommittee that:

> The Department of Justice has long predicated its enforcement efforts in export related matters upon the ability to prove a substantial and foreseeable effect on U.S. commerce. (Id. at pp. 154–155)

This interpretation of existing antitrust law was confirmed by Sanford Litvack, Assistant to Attorney General, Antitrust Division. In a letter to Senator Proxmire, Chairman of the Committee on Banking, Housing, and Urban Affairs, Mr. Litvack noted that certain activities undertaken by exporters "may well not violate the Sherman Act in any event *due to their lack of substantial effect on U.S. trade or commerce.*" (emphasis supplied)

These interpretations of existing antitrust law are consistent with long standing policy. For example, the 1955 Report of the Attorney General's Antitrust Committee stated:

> We feel that the Sherman Act applies only to those arrangements between Americans alone, or in concert with foreign firms, which have such substantial anticompetitive effects on this country's trade or commerce * * * with foreign nations' as to constitute unreasonable restraints. (Report, supra at pp. 76–77).

The bill also adds two new substantive standards, requested by the Department of Justice, to the Webb-Pomerene Act—a requirement that the export trade must not constitute trade or commerce in the licensing of patents, technology, trademarks or know-how, and that the export activities must serve to preserve or promote export trade.

Before an association or export trading company can obtain certification, the Secretary of Commerce also must find that the export activities to be certified will serve a specified need. Only those export trade, export trade activities and methods of operation specified in the certification issued by the Secretary of Commerce are immunized. The certification must include any terms or conditions deemed necessary by the Secretary, in consultation with the Department of Justice and the Federal Trade Commission, in order to bring the company or its export activities into compliance with any of the substantive standards. Any material change in the export trade, export trade activities or methods of operation must be reported to the Secretary and any modification to the certification must be approved by the Secretary. The guidelines to be used in making these determinations are to be issued by the Secretary of Commerce, after consultation with the Attorney General and the Federal Trade Commission.

8. Amendment, Revocation or Invalidation

Even after the export activities of an association or export trading company have been certified, they remain subject to the continuing scrutiny of the Department of Commerce and Justice and the Federal Trade Commission. The certification of any association or export trading company whose activities fail to comply with any of the substantive standards is subject to modification or revocation by the Department of Commerce. Additionally, either the Department of Justice or the Federal Trade Commission at any time may initiate an action to invalidate all or any part of the certification of an association or trading company. Once the certification has been revoked, civil or criminal actions and enforcement proceedings may be brought on a prospective basis.

TITLE III—TAXATION OF EXPORT TRADING COMPANIES

9. Application of DISC Rules

The tax provisions have two purposes: (1) to enable export trading companies to use DISC with respect to all their income from exports of services as well as products; and (2) to permit small, closely held companies to use Subchapter S to pass through net losses in the first few years when start-up costs are likely to exceed income. If there is any significant revenue loss directly attributable to the tax provisions, it will be because export trading companies succeed in significantly expanding U.S. exports, which means additional revenue is being produced through additional exports.

Section 301 would provide that gross receipts of an export trading company from "export trade services" as well as the export of "services produced in the United States," as defined in the Act, are eligible DISC receipts. The purpose of the provision is to avoid forcing export trading companies to segregate artificially certain services in order to enjoy DISC status for the receipts from such services.

This section would also require the Assistant Secretary of Commerce, with the cooperation and assistance of the Director of the Internal Revenue Service to disseminate information to exporter and export trading companies on how to form and use DISCs.

The Treasury Department computed the potential revenue cost of extending DISC benefits to "services produced in the United States" at $740 million for 1978. Acknowledging the difficulties of computing the actual revenue cost, this figure was reduced to a "more conservative estimate of $200–500 million." Similarly, Treasury noted that the potential revenue cost of extending DISC benefits to "export trade services" as $200 million, reduced to "a conservative ball park estimate of $100–200 million."

However, Treasury's computations were based on the premise that DISC benefits would be extended to the services produced in the U.S. or the export trade services of all DISC's. The bill extends DISC treatment of these services only to DISCs which are export trading companies. Thus, to the extent Treasury's estimates are based on income from DISC's which would not qualify as export trading companies, the estimates necessarily overstate the actual revenue costs. Since most DISC's are exporting, either solely or principally, the goods or services of a parent or affiliate, the number of present DISC's which would qualify as export trading companies is likely to be relatively small.

10. Subchapter S Status

Section 302 would amend Subchapter S of the Tax Code to permit an export trading company to use the provisions of that subchapter without limiting the foreign source income of such company to less than 20 percent per annum. Some export trading companies might have difficulty complying with the existing statutory restriction. Section 302 would also permit shareholders in companies eligible to use subchapter S to be not more than 15 individuals or companies, if the companies are each owned by not more than 15 individuals.

Section-by-Section Analysis of the Bill

TITLE I—EXPORT TRADING COMPANIES

Short Title

Section 101 provides that Title I may be cited as the "Export Trading Company Act of 1980."

Findings

Section 102 includes eight findings by Congress concerning exports and export trading companies, and states that the purpose of the Act is to increase U.S. exports by encouraging more efficient provision of export trade services to U.S. producers.

Definitions

Section 103 defines the following terms used in the title: "export trade," "goods produced in the United States," "services produced in the United States," "export trade services," "export trading company," "United States," "Secretary," and "company." An export trading company is defined as a U.S. company "organized and operated principally for the purposes of (A) exporting goods or services produced in the United States; and (B) facilitating the exportation of goods and services produced in the United States by unaffiliated persons by providing one or more export trade services."

Promotion of Export Trading Companies by Secretary of Commerce

Section 104 requires the Secretary to promote and encourage formation and operation of export trading companies by providing information and advice to interested persons and by facilitating contact between producers and firms offering export trade services.

Definitions in Section on Bank Ownership

Section 105(a) defines "banking organization," "State bank," "State member bank," "State nonmember insured bank," "bankers' bank," "bank holding company," "Edge Act Corporation," "Agreement Corporation," "appropriate Federal banking agency," "capital and surplus," "affiliate," "control," "subsidiary," and "export trading company." The terms "control" and "subsidiary" are defined as in the Bank Holding Company Act. The term "export trading company" means an export trading company as defined in sec. 103(5) or a company organized and operated principally for the purpose of providing export trade services.

Authority to Own Export Trading Companies

Section 105(b)(1) would authorize banking organizations, subject to the procedures and limitations of section 105 (b) and (c) to invest in the aggregate not more than 5 percent of the banking organizations consolidated capital and surplus in export trading companies.

Section 105(b)(1)(A) would authorize investments of up to $10 million in total by a banking organization without prior approval by the appropriate Federal banking agency if such investment did not make the export trading company a subsidiary of the banking organization (Pursuant to the Bank Holding Company Act, ownership of 25 percent of the stock is presumed to constitute control and therefore make the company a subsidiary, and ownership of less than 25 percent may be found by the Federal banking agency to constitute control and make the company a subsidiary. If the agency made such finding it could require divestiture or place conditions on the investment.). Section 105(b)(1)(B) would permit investments of more than $10 million, or controlling investments, or investments which give a group of banking organizations more than 50 percent of the stock of an export trading company, only with prior approval of the appropriate Federal banking agency.

Section 105(b)(2) would require banking organizations to notify the appropriate Federal banking agency 60 days before making any additional investment in an export trading company subsidiary or engaging in any line of activity, including specifically the taking of title to goods, which was not previously disclosed. The Federal banking agency could disapprove or place conditions on such investment or activity.

Section 105(b)(3) would provide that if the appropriate Federal banking agency failed to act upon an application or notification within the specified time period, approval would be assumed.

Additional Limitations on Bank Investments in Export Trading Companies and on Such Companies

Section 105(c) would place the following limitations on export trading companies and investments in them by banking organizations: (1) the export trading company could not use a name similar to that of any banking organization owning any of its stock; (2) the total historical cost of a banking organization's direct and indirect investments in an export trading company, plus any credit extended by the organization and its subsidiaries to the company, could not exceed 10 percent of the banking organization's capital and surplus; (3) banking organizations could not hold stock in export trading companies which take speculative positions in commodities; and (4) banking organizations could not extend credit to any export trading company in which it holds stock, or to the company's customers, on terms "more favorable than those afforded similar borrowers in similar circumstances, and such extension of credit shall not involve more than the normal risk of repayment or present other unfavorable features."

Factors to be considered by Federal Banking Agencies in Disapproving or Placing Conditions on Investments

Section 105(d) would require the appropriate Federal banking agency to consider the resources, competitive situation, and future prospects of the banking organization and export trading company concerned in any application, and the effect on United States competitiveness in world markets, and authorize the agency to disapprove the investment if it finds the export benefits are "outweighed in the public interest by adverse financial, managerial, competitive, or other banking factors." The agency would be authorized to impose such conditions on approved investments or activities as it deemed necessary" (A) to limit a banking organization's financial exposure to an export trading company, or (b) to prevent possible conflicts of interest or unsafe or unsound banking practices." The agency would be required to set standards for the taking of title to goods and holding of inventory to prevent unsafe or unsound practices. In imposing conditions, the Federal banking agency would be required to consider the size of the banking organization and export trading company involved, the degree of investment or other support to be provided by the banking organization, and identity and financial strength of other investors. The agency could not impose conditions on the taking of title which unnecessarily disadvantage, restrict or limit trading companies in competing in world markets. Not withstanding any other provision, the appropriate Federal banking agency could after due notice and opportunity for hearing, order an investment in an export trading company terminated if the agency had reasonable cause to believe the investment constituted a serious risk to the banking organization or was inconsistent with sound banking principles or the Financial Institutions Supervisory Act of 1966. Within two years after enactment a report to Congress by the Federal banking agencies would be required.

Court Appeals

Section 105(e) would provide an opportunity to appeal orders of Federal banking agencies to the Federal Court of Appeals and require cases of procedural error to be remanded to the agency and permit cases of substantive error to be remanded to the agency as well.

Rulemaking and Enforcement

Section 105(f) would provide general rulemaking authority to Federal banking agencies for purposes of administering this section.

Initial Investments and Operating Expenses

Section 106 would direct EDA and SBA to give special weight to export benefits, including opening new export markets and encouraging exporting by small and medium-size businesses or agricultural concerns, when considering applications by export trading companies for loans and guarantees. $20 million would be authorized to be appropriated for each of the next 5 fiscal years for the purposes of this section.

Guarantees for Export Accounts Receivable and Inventory

Section 107 would direct the Export-Import Bank to establish a guarantee program for commercial loans secured by export accounts receivable or inventories of exportable goods when the Bank's Board judged the private credit market was not providing adequate export financing to otherwise creditworthy exporters and such guarantees would facilitate exports which would not otherwise occur. The guarantees would be subject to limits in annual appropriation Acts.

TITLE II—EXPORT TRADE ASSOCIATIONS

Section 201. Short Title: Export Trade Association Act of 1980

Finding and Declaration of Purposes

Section 202 sets forth findings by the Congress regarding exports and joint exporting activities and the purposes of the Act.

Definitions

Section 203 defines the pertinent terms. The definition of "export trade" is expanded from the definition contained in the Webb-Pomerene Act (15 U.S.C. 61–66) to include services. The term "service" means intangible economic output, including, but not limited to business, repair, and amusement services; management, legal, engineering, architectural, and other professional services; and financial, insurance, transportation, and communication services. The term "export trade activities" includes any activities or agreements in the course of export trade. The term "association" refers to any combination of persons, partnerships, or corporations, all of which must be citizens of the United States or created under the laws of any State or of the United States. A foreign controlled subsidiary created under the laws of any State or of the United States, however, cannot be a member of the "association." The term "antitrust laws" means the antitrust laws defined in the first Section of the Clayton Act and Section 4 of the Federal Trade Commission Act.

Exemption from Antitrust Law

Section 204 strikes Sections 2 and 4 of the Webb-Pomerene Act and inserts in lieu thereof a new Section 2. Section 2 provides that an export trade association or export trading company and their members, certified according to the procedures set forth in this Act is exempt from the application of the antitrust laws during the period of the certification provided that the association or export trading company and its export trade activities (1) serve to preserve or promote export trade; (2) neither result in a substantial lessening of competition or substantial restrain of trade within the United States nor constitute a substantial restraint of the export trade of any competitor of the association; (3) do not unreasonably enhance, stabilize, or depress prices within the United States; (4) do not constitute unfair methods of competition against competitors engaged in export trade; (5) are not reasonably expected to result in the consumption or resale in the United States of goods or services exported by the association or export trading company; and (6) do not constitute trade or commerce in the licensing of patents, technology, trademarks, or know-how, except as incidental to the sale of goods or services exported by the association or export trading company or its members.

Section 2 also provides for a 30 day suspension of the effective date of the exemption if the Attorney General or the Federal Trade Commission formally advises the Secretary of Commerce that it disagrees with the Secretary's determination to issue a certification.

Section 205. Conforming Changes in Style Section 205 amends Section 3 of the Webb-Pomerene Act to provide for conforming change in style.

Administraton; Enforcement; Reports

Section 206 strikes Section 5 from the Webb-Pomerene Act and inserts in lieu thereof a new Section 4 and eight additional new sections.

A new Section 4(a) establishes the procedure for applying for certification as an export trade association or export trading company. It requires associations or export trading companies seeking certification to file applications describing in detail their proposed export activities including the goods or services to be exported, the methods of export trade, including, but not limited to, any agreements to sell exclusively to or through the association, any agreements with foreign persons who may act as joint selling agents, any agreements to acquire a foreign selling agent, any agreements for pooling tangible or intangible property or resources, or any territorial, price-maintenance, membership, or other restrictions to be imposed upon members of the association or export trading company, and any other information the Secretary may request on the association or company, its relations with other associations or companies, and effects on competition or potential competition.

A new Section 4(b) requires the Secretary to certify an association or export trading company within 90 days after receiving the application if the Secretary determines, after consultation with the Attorney General and Federal Trade Commission, that the proposed trade activities and methods of operation meet the standards set forth in amended Section 2 of the Act and will serve a specified need in promoting export trade. The certificate must specify permissible activities and any terms and conditions deemed necessary to ensure that the standards of the Act are met. Expedited certification and appeals procedures are specified.

This Section also requires the Secretary to provide the Attorney General and the Federal Trade Commission with a copy of the proposed certificate and sets forth procedures to be followed by the Attorney General and the Commission in rendering advice on a certification. Certifications may be issued by the Secretary prior to the expiration of forty-five days after the proposed certification has been delivered to the Attorney General or the Commission only if no formal notice of disagreement has been made by the Attorney General or Commission under the procedures specified in the Act.

A new Section 4(c) of the Webb-Pomerene Act requires certified export trade associations and export trading companies to report any material changes in membership, export trade, export trade activities and methods of operations and allows them to apply for an amended certificate. There is no interruption in the certification period for applications made within 30 days of the change and approved by the Secretary.

A new Section 4(d) of the Act permits the Secretary to require certified export trade associations or export trading companies to modify their organization or operation to correspond with their certification, or to revoke or amend the certification.

A new Section 4(e) to the Webb-Pomerene Act authorizes the Attorney General or Federal Trade Commission to bring an action to invalidate, in whole or in part, a certification on the grounds that the export trade, export trade activities or methods of operation of an export trade association or export trading company fail to meet the standards of Section 2 of the Act. This Section also permits the Attorney General or Commission to seek preliminary relief pending the disposition of an action if the Attorney General or Commission brings an action for invalidation the 30 day period provided in Section 2(b)(2). No person other than the Attorney General or the Commission would have standing to bring an action against an association or company for failure to meet the standards of Section 2 of the Act.

A new Section 5 to the Webb-Pomerene Act requires that the Secretary, the Attorney General, and the Chairman establish guidelines for purposes of determining whether an association, its members and its export trade activities meet the requirements of the new Section 3.

A new Section 6 to the Webb-Pomerene Act stipulates that every certified association or export trading company shall submit to the Secretary an annual report setting forth the information required in the application for certification.

A new Section 7 to the Webb-Pomerene Act establishes within the Department of Commerce an office to promote and encourage to the greatest extent feasible for formation of export trade associations through the use of provisions of this Act.

A new Section 8 to the Webb-Pomerene Act provides for automatic certification for existing export trade association registered under current law. In order to obtain automatic certification, an existing export trade association must file and application for certification with 180 days after the date of enactment of this Act.

A new Section 9 to the Webb-Pomerene Act provides for the confidentiality of the information contained in an association's application for certification, application for amendment of certification, and annual report.

Section 9 also requires the Secretary to make available to the Attorney General and the Commission for their official use all materials filed by an association or export trading company which has been certified or, which has applied for certification if the Secretary believes the applicant is eligible for certification.

A new Section 10 to the Webb-Pomerene Act authorizes the Secretary of the Treasury to require an association or export trading company to modify its operations so as to be consistent with future international obligations of the United States set by treaty or statute.

A new Section 11 to the Webb-Pomerene Act authorizes the Secretary, in consultation with the Attorney General and the Chairman, to promulgate such rules and regulations as are necessary to carry out the purposes of this Act.

A new Section 12 to the Webb-Pomerene Act requires the President seven years after the date of enactment of this Act to appoint a task force to examine the effect of the operation of this Act on domestic competition and on the United States' international trade deficit and to recommend either continuation, revision, or termination of the Webb-Pomerene Act.

Section 6 of the Webb-Pomerene Act is redesignated as "Section 14. Short Title".

TITLE III: TAXATION OF EXPORT TRADING COMPANIES

DISC

Section 301 would amend the provisions of The Internal Revenue Code concerning Domestic International Sales Corporations (DISCs) in order to: (a) insure that bank investments in export trading companies would not disqualify such companies from using DISCs; (b) make receipts from exports of services or export trade services eligible DISC receipts, that is, eligible for partial deferral of income taxation; and (c) require the Secretary of Commerce in consultation with the Secretary of the Treasury to prepare and distribute information on how export trading companies could use DISC status and the likely advantages or disadvantages of doing so.

Subchapter S

Section 302 would amend provisions of subchapter S of the Internal Revenue Code which permit closely held corporations (15 or fewer individual shareholders) to pass through certain losses or income to shareholders. The amendments would exclude export trading companies from the requirement that 20 percent of the annual income of a subchapter S corporation be domestic income, and permit an export trading company to qualify for subchapter S if owned by shareholders which were small business corporations as defined in subchapter S authorizing in effect a second-stage subchapter S corporation.

Fiscal Impact Statement

In accordance with section 252(a) of the Legislative Reorganization Act of 1970, the Committee estimates the bill will result in additional outlays during fiscal year 1981 of $15,000,000. This concurs with the estimate prepared by the Congressional Budget Office, which follows:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, D.C., May 15, 1980.

Hon. WILLIAM PROXMIRE,
Chairman, Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Pursuant to Section 403 of the Congressional Budget Act of 1974, the Congressional Budget Office has prepared the attached cost estimate for a bill to encourage exports by facilitating the formation and operation of export trading companies, export trade associations, and the expansion of export trade services generally, as ordered reported on May 12, 1980.

Should the Committee so desire, we would be pleased to provide further detail on the attached cost estimate.

Sincerely,

ALICE M. RIVLIN,
Director.

CONGRESSIONAL BUDGET OFFICE—COST ESTIMATE

1. Bill number: Not Yet Assigned.
2. Bill title: A bill to encourage exports by facilitating the formation and operation of export trading companies, export trade associations, and the expansion of export trade services generally.
3. Bill status: Committee Print No. 2 as ordered reported by the Senate Committee on Banking, Housing, and Urban Affairs on May 12, 1980.
4. Bill purpose: The purpose of Title I is to encourage more efficient provision of export trade services to American producers and suppliers. Section 106 directs the Economic Development Administration and the Small Business Administration to give special weight to export-related benefits when considering loan and guarantee applications by export trading companies. In addition, it authorizes the annual appropriation of $20 million for fiscal years 1981 through 1985 for this purpose. Section 107 directs the Export-Import Bank to establish a program to provide loan guarantees to export trading companies. These loan guarantees are subject to the limitations provided in the annual appropriation acts.

Title II applies the Webb-Pomerene Act to the exportation of services and transfers the Administration of that Act from the Federal Trade Commission to the Secretary of Commerce. Section 205 establishes an office within Commerce to encourage the formation of export trade associations. In addition, the section requires that a task force be appointed seven years after enactment of this bill to examine the effect of these trade associations.

Title III applies the Domestic International Sales Corporation (DISC) rules to export trading companies and directs the Secretary of Commerce to prepare and distribute information on the application of these rules.

5. Cost estimate:

	Millions
Authorization amount:	
Fiscal year:	
1981	$20
1982	20
1983	20
1984	20
1985	20
Estimated outlays:	
Fiscal year:	
1981	15
1982	20
1983	20
1984	20
1985	20

6. Basis of estimate: This estimate assumes enactment of this legislation before October 1, 1980. It further assumes that the annual authorization amounts will be appropriated in full in the year authorized.

The only direct budget cost estimated for the bill occurs in Title I which authorizes the annual appropriation of $20 million to the Economic Development Association and Small Business Administration. Outlays were derived by applying a composite outlay rate. Loan guarantees of the Export-Import Bank are assumed to be provided within the annual limitation on program activity. In any case, guarantees are estimated not to be drawn and therefore result in no budget authority or outlays.

While Title II creates an office within the Department of Commerce, there is no authorization for appropriation for the office. It is assumed, therefore, that funds for this office will be transferred or reprogrammed to fulfill this section. The task force requirement is beyond the projection period; no costs are included for this provision.

The provisions of Title III, allowing certain export trading companies to be treated as DISCs, will reduce corporate profit tax receipts. In the time available, however, CBO has not been able to estimate the amount of the reductions.

7. Estimate comparison: None.
8. Previous CBO estimate: None.
9. Estimate prepared by: Rita Seymour and Rosemary Marcus.
10. Estimate approved by:

C. G. NUCKOLS,
(For James L. Blum,
Assistant Director for Budget Analysis).

EVALUATION OF REGULATORY IMPACT

In the opinion of the Committee, it is necessary to dispense with the Rules of the Senate, the Committee has evaluated the regulatory impact of this bill. The Committee concludes that the bill will have no additional regulatory impact.

CHANGES IN EXISTING LAW

In the opinion of the Committee, it is necessary to dispense with the requirements of section 4 of Rule XXIX of the Standing Rules of the Senate in order to expedite the business of the Senate.

COMPTROLLER OF THE CURRENCY,
ADMINISTRATOR OF NATIONAL BANKS,
Washington, D.C., May 12, 1980.

Hon. WILLIAM PROXMIRE,
Chairman, Committee on Banking, Housing and Urban Affairs, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the views of the Office of the Comptroller of the Currency (OCC) on the proposed "Export Trading Company Act of 1980", S. 2379.

The proposed legislation promotes the expansion of U.S. exports by permitting the formation and operation of export trading companies ("ETCs"), which would facilitate the marketing and export of goods and services on behalf of small and medium sized U.S. firms. S. 2379 also proposes a leading role for U.S. banks informing and operating ETCs.

The OCC strongly supports S. 2379 with certain reservations. The OCC believes in the need to expand U.S. exports, as well as in the benefits of employing the national and international marketing and financial networks of U.S. banks for export expansion. Bank ownership of ETCs does raise supervisory concerns; however, the OCC believes the proposed legislation can be amended to address those concerns while still permitting a leading role for banks in ETCs.

Specifically, the OCC's primary concern is the degree of exposure a bank-owned ETC may raise for the bank investor. Exposure can be the amount of loans and investment a bank provides an ETC. However, exposure also can include a bank's moral obligations on behalf of a subsidiary which is closely identified with the bank through equity participation, and borrows in the marketplace on the basis of that equity interest.

Accordingly, the OCC suggests the proposed S. 2379 be amended to recognize these supervisory concerns. This Office especially recommends during this threshold stage of ETC development that the proposed legislation permit a banking organization to invest the lower of $10 million or five percent of its consolidated capital funds in less than twenty-five percent of the equity of an ETC without the prior approval of the appropriate federal banking agency. Aggregate bank investments in ETCs should be limited to 10 percent of a banking organization's consolidated capital funds. At a minimum, any investments by banks in ETCs which require prior approval should be subject to whatever safety and soundness conditions the appropriate banking agency may wish to impose.

Sincerely,

JOHN G. HEIMANN,
Comptroller of the Currency.

THE SECRETARY OF COMMERCE,
Washington, D.C., May 12, 1980.

Hon. ADLAI E. STEVENSON,
U.S. Senate,
Washington, D.C.

DEAR ADLAI: This letter supplements my April 3, 1980, testimony on S. 2379 and S. 864 with a more detailed Administration position on an antitrust exemption for export trade activities.

As you know, I reported during my April 3 testimony that the Administration had been unable to agree on the form of participation by the Justice Department in the process of certifying certain export activities to be exempt from application of the antitrust laws. Since that time, extensive consultations among the Commerce Department, USTR, the Justice Department, and other agencies have led to Administration agreement upon the form of that participation. Accordingly, I am pleased to state on behalf of the Administration that, with the few changes I have noted below, we could support an antitrust provision for export trade associations and export trading companies such as that contained in title II of the draft committee print of May 3, 1980. (The Administration has not yet considered whether the antitrust exemption should be applicable, as proposed in the May 3 print, to individual companies, other than export trading companies, which are not part of an export trade association.)

1. The Administration believes that the Attorney General and the Federal Trade Commission should have an opportunity to review any certificate that the Commerce Department proposes to issue before that certificate becomes effective. This review would allow for consultations between the Commerce Department and the antitrust enforcement agencies in an effort to avoid issuing certificates for activities that would have anti-competitive effects in the United States. The Commerce Department would be free to issue a certificate even if an antitrust agency objected. However, when such an objection had formally been lodged, the antitrust exemption provided for in the certificate would not take effect for thirty days. I have enclosed language drafted by the Administration to implement this principle.

2. The Administration believes that the Attorney General or the Federal Trade Commission should be able to seek preliminary relief during this thirty-day period to prevent the antitrust exemption from taking effect. Normal judicial standards for preliminary relief in antitrust cases would apply. Therefore, the following language, which appears in other antitrust laws, should be included in the provision for invalidation of the certificate by the Attorney General or the Commission:

> Pending such action, and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises.

In this regard, the provision requiring thirty-day notice before an antitrust agency institutes an action for invalidation is inappropriate and should not apply in the case of an action brought in any thirty-day period before an exemption takes effect.

3. In order for the antitrust enforcement agencies to comment knowledgably upon the competitive consequences of granting a certificate,

these agencies must have the information provided by applicants for certificates. However. the agencies need this information only where they will actually be called upon to comment. Accordingly, the following language should be included in the beginning of the provision on discosure of information to the Attorney General and the Commission:

> Whenever the Secretary believes that an applicant may be eligible for a certificate, or has issued a certificate to an association or export trading company, he shall promptly make available all materials filed by the applicant, association or export trading company, including applications and supplements thereto, reports of material changes, applications for amendments and annual reports, and information derived therefrom.

We are, of course, prepared to assist you or the Committee in any way in drafting suitable language or in rectifying the minor drafting problems in the current draft committee print.

Sincerely,

PHILIP W. KLUTZNICK,
Secretary of Commerce.

FEDERAL RESERVE SYSTEM,
Washington, D.C., May 12, 1980.

Hon. ADLAI E. STEVENSON,
U.S. Senate,
Washington, D.C.

DEAR SENATOR STEVENSON: My letter to you of May 2 expressed certain reservations regarding S. 2379. Those reservations stem not from lack of sympathy with the purpose of this legislation in making export related services available to more firms in the U.S. Rather, we in the Federal Reserve have substantial questions about the degree to which banking organizations should be permitted to participate directly in, or even control, export trading companies. In that connection, we feel strongly that the tradition of separation of banking and commerce has served the country well. To assure that separation is maintained, while permitting a degree of banking participation in support of export trading companies. I would suggest certain amendments to the proposed bill establishing substantive and procedural standards that are necessary with regard to bank involvement in such companies.

Those recommendations, which I endorse, include the following elements: first, no banking organization would be permitted to acquire more than 20 per cent of the voting stock of an export trading company or to control the company in any other manner; second, not more than 50 per cent of an export trading company's voting stock could be owned by any group of banking organizations; third, the aggregate investment by any banking organization would be limited to 5 per cent of its aggregate capital and surplus (25 per cent in the case of Edge and Agreement Corporations) in one or more export trading companies nor could a banking organization lend to an export trading company in an amount which, when combined with its investment, would exceed 10 per cent of the banking organization's capital and surplus; an export trading company would not be permitted to take positions in securities or commodities for speculative purposes; an arms length relationship would be maintained in any lending activity; and the name of the bank could not be used in the name of the export trading company.

Furthermore, we propose that any major commitment to investment in an export trading company—in excess, say, of $10 to $15 million—be specifically approved by the Board of Governors in advance. As this suggests, we believe that because of the risks that may attend export trading company activities and the lack of experience of U.S. banks and their regulators in dealing with such companies, it would not be prudent to permit banking organizations to exercise control over export trading companies at this time. For that reason, the Board of Governors cannot support the current version of S. 2379.

The amendments that I am enclosing for the Committee's consideration have been discussed with your staff. We, of course, would be pleased to provide any further assistance.

Sincerely,

PAUL A. VOLCKER.

ADDITIONAL VIEWS OF SENATOR WILLIAM PROXMIRE

I find it unfortunate that important banking legislation was reported by the Committee on Banking, Housing and Urban Affairs without the Committee having had the benefit of appearance before it of the bank regulatory agencies charged with the safety and soundness of the banking system.

Unquestionably it would have been inconvenient for the movers of this legislation to have heard first hand the doubts of the banks regulatory agencies which bear the ultimate responsibility for underwriting the liquidity and solvency of the banking system.

But the inconvenience of listening to responsible contrary views just might have given the Senate a better understanding of the magnitude of this legislation and its potential effect of the public interest.

Let us make no mistake about it, this is major banking legislation. It breaks the demarcation between banking and commerce because it allows banks to take controlling equity positions in export-import companies, trading goods of production and commodities. Historically, banking and commerce have been separated by law in this country. This has been so for over 100 years for good reason. Banks play a significant role in the life of our economy by safeguarding the Nation's savings and providing the lifeblood of our economic system: credit. Credit judgments should be made on the merits. Arms length dealing in the credit mechanism has been ensured by the traditional separation of banking and commerce.

When a bank has a stake in economic enterprise its credit judgments tend to be skewed. The most recent example is the involvement of banks in the real estate inevstment trust business where bank losses ran to the hundreds of millions of dollars. Congress, in fact, had to adopt special legislation just this year to bail out large banks holding real estate in connection with REIT defaulted loans, so that those banks would not have to charge off large losses to their already depleted capital base. Now, the same big banks are to be given the power to engage in lines of commerce in which they have no expertise.

This legislation gives rise to identical risks to the banking industry which came out of the REIT experience, only the risks are far greater this time. The ramifications of this legislation are enormous. Banks would be permitted to take controlling equity positions in Export Trading Companies. A bank owned Export Trading Company would be permitted to engage in a wide range of export-import transactions. Such a bank owned Export Trading Company would be permitted to contract to build a textile mill in China, purchasing the equipment both in the U.S. and overseas. In payment for the mill, the Export Trading Company could take oil in a barter transaction, ship the oil to the U.S. market on tankers which it would be permitted to own, and market the oil in the U.S. The bank owned Export Trading Company could purchase wheat or grain in the forward market for sale in international markets pursuant to their marketing efforts. Such an Export Trading Company would be permitted to engage in the travel agency business overseas and for travel to and from the United States; amusements for export would be permitted, no doubt including motion pictures.

While banks may provide a useful service to Export Trading Companies in providing financing and financial services to exporters, it is clear to me that banks have no expertise to offer in actual construction projects, purchase and sale of commodities and barter transactions which may include exporting a truck factory and importing vodka in payment.

Thus, while I remain skeptical of the entire Export Trading Company concept for banks at all, I can understand that perhaps to facilitate the financial aspects of export-import transactions banks may need to have a non-controlling position in an Export Trading Company.

That is why I supported the Federal Reserve Board amendment prohibiting bank control of Export Trading Companies and which would have restricted any bank's investment in an Export Trading Company to a non-controlling interest, not to exceed 20 percent of the Export Trading Companies stock and to restrict the interest of several banks in a single Export Trading Company to under 50 percent. The Federal Reserve amendment—which was supported by the Federal Deposit Insurance Corporation—would have retained the benefits of bank participation in Export Trading Companies while avoiding the pitfalls associated with bank control of commercial enterprises.

The pitfalis are substantial. At a time when the banking system is undercapitalized and with the shortage of capital being particularly acute at large banks, the needs of a soundly capitalized banking system require at the largest banks that banks not be encouraged to drain capital away from their credit function. We should remember all to well the unfortunate consequences of the recent era of "go-go" banking and REITs and not encourage banks to stray from their essential economic purpose which is to provide financing for productive purposes.

Controlling equity investments in lines of commerce holds the probability that the public will suffer the consequences as it did in the REIT experience and "go-go" banking of recent years. Those consequences include the need for Congress to pass special legislation to allow banks extended time to hold real estate held in connection with defaulted loans made for speculative lending purposes; Federal Reserve lending to prevent bank failures; and ultimate FDIC funding to prevent deposit payouts by banks in receivership.

It is clear to me that in breaching the 100 year old separation between banking and commerce that prudence dictates caution. The Federal Reserve amendment would have allowed bank participation in Export Trading Companies while ensuring the prevention of the type of abuses associated with bank expansion into nonbanking activities. The virtue of the Federal Reserve amendment is that it would have given the Congress the option down the road in a year or two based upon the record of limited bank participation in Export Trading Companies to determine whether the public interest would be at all served by bank control of Export Trading Companies. The Committee has made this judgment now, prematurely in my view, without even the benefit of bank regulatory agency participation in open hearings.

This legislation also contains amendments to the Internal Revenue Code which lie completely outside this Committee's jurisdiction. The tax provisions to which I refer would make Export Trading Companies with bank ownership eligible for DISC tax treatment; make receipts from export trade services eligible for DISC tax benefits; and would exclude Export Trading Companies from the requirements of Subchapter S relating to closely-held corporations requiring that 20 percent of such a corporation's annual income be domestic income. I am afraid that the Committee's action on the tax code is another example of the questionable procedures that have been followed in considering this bill. That bill should not be considered at all by the Senate until the tax writing committees have given detailed consideration to these tax provisions.

On substantive grounds, I join with the Administration in opposing this major expansion of the tax benefits afforded to export activities.

In the most recent Committee hearings on this legislation, Commerce Secretary Klutznick, giving the Administration's position, stated the following:

> Many, if not all, ETCs should be able to meet the requirements of present DISC legislation and benefit from DISC tax deferral status. Modification of U.S. banking laws to permit bank ownership of export trading companies will effectively expand DISC coverage without requiring any change in the DISC statute itself. However, to amend DISC legislation to cover exports of all services, as well as services provided by other U.S. firms to export trading companies, as S. 2379 would do, would definitely alter the nature and scope of the DISC program and substantially increase its revenue costs. The present realities of the budget situation do not permit such an extension at this time. I could also raise questions about our international obligations in this area and our concerns for tax equity.

Assistant Treasury Secretary Bergsten subsequently provided the Committee with a more detailed statement of the Administration's position and with estimates of the potential impact of Title III on tax revenues. Giving what were styled as "conservative estimates," the Bergsten letter stated that the extension of DISC benefits to "services produced in the United States" could result in revenue losses of $200 to $500 million and similar coverage of "export trade services" could cost the Treasury $100–$200 million. I also agree with the Administration's opposition to the amendments to Subchapter S contained in Title II on the ground that any legislation of this sort should be considered within the context of the proposal by the Joint Committee on Internal Revenue Taxation to overhaul Subchapter S. This seems to me to be perfectly reasonable and in fact far preferable to precipitous actions by this Committee.

Lastly, this legislation contains a major revision to the Webb-Pomerene Act which now contains a limited exception to the proscriptions of the Sherman Act for joint ventures which are limited to exports. I know that the authors did not intend to make substantive changes in the Webb-Pomerene exceptions. Nevertheless, I believe the Senate would have been better served if the Judiciary Committee—with its antitrust expertise—had reviewed these provisions in hearings. Once again, the procedure followed here to rush a bill to the Senate floor may not serve the public interest well. Antitrust laws are complicated and they deserve careful consideration. Especially is this so with respect to this bill which ousts the Justice Department Antitrust Division out of the Administration of the Webb-Pomerene Act in favor of the Commerce Department. With all due respect to the Commerce Department, I think it fair to say that it has no expertise at all in enforcing the antitrust laws. In my judgment, it is no answer to say that if Commerce makes a mistake Justice can sue them in the courts. Courts are not administrators. Enforcement action will be at the desk in Commerce which reviews the application for exceptions to the antitrust laws. The Senate needs to ask itself if the public deserves the defanging of the Antitrust Division of the Justice Department, especially in the light of the fact that upon Commerce Department approval carries with it immunity from suit by private parties and state attorneys general on behalf of persons who might have been injured by reason of agreements in restraint of trade.

WILLIAM J. PROXMIRE.

FEDERAL RESERVE SYSTEM,
Washington, D.C., May 12, 1980.

Hon. WILLIAM PROXMIRE,
Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate, Washington, D.C.

DEAR CHAIRMAN PROXMIRE: My letter to you of May 2 expressed certain reservations regarding S. 2379. Those reservations stem not from lack of sympathy with the purpose of this legislation in making export related services available to more firms in the U.S. Rather, we in the Federal Reserve have substantial questions about the degree to which banking organizations should be permitted to participate directly in, or even control, export trading companies. In that connection, we feel strongly that the tradition of separation of banking and commerce has served the country well. To assure that separation is maintained, while permitting a degree of banking participation in support of export trading companies, I would suggest certain amendments to the proposed bill estabilshing substantive and procedural standards that are necessary with regard to bank involvement in such companies.

Those recommendations, which I endorse, include the following elements: first, no banking organization would be permitted to acquire more than 20 percent of the voting stock of an export trading company or to control the company in any other manner; second, not more than 50 percent of an export trading company's voting stock could be owned by any group of banking organizations; third, the aggregate investment by any banking organization would be limited to 5 percent of its aggregate capital and surplus (25 percent in the case of Edge and Agreement Corporations) in one or more export trading companies nor could a banking organization lend to an export trading company in an amount which, when combined with its investment, would exceed 10 percent of the banking organization's capital and surplus; an export trading company would not be permitted to take positions in securities or commodities for speculative purposes; an arms length relationship would be maintained in any lending activity; and the name of the Bank could not be used in the name of the export trading company.

Furthermore, we propose that any major commitment to investment in an export trading company—in excess, say, of $10 to $15 million—be specifically approved by the Board of Governors in advance. As this suggests, we believe that because of the risks that may attend export trading company activities and the lack of experience of U.S. banks and their regulators in dealing with such companies, it would not be prudent to permit banking organizations to exercise control over export trading companies at this time.

The amendments that I am enclosing for the Committee's consideration have been discussed with your staff. We, of course, would be pleased to provide any further assistance.

Sincerely,

PAUL A. VOLCKER.

ADDITIONAL VIEWS OF SENATORS TOWER, CRANSTON, AND GARN

The purpose of the Export Trading Company Act of 1980, as stated in Sec. 102(b) thereof, is to increase United States exports of products and services by encouraging more efficient provision of export trade services to American producers and suppliers. We fully support this objective. The sooner our merchandise trade balance becomes a surplus rather than a deficit, the healthier our economy will be.

We are concerned, however, that this bill provides a significant departure in the manner in which our financial institutions have traditionally operated. Throughout our history, commercial banks have financed commercial activities. They have not maintained ownership interests in commercial ventures. There are many questions that have been raised by the provision in the bill allowing banking organizations to obtain ownership interests in commercial ventures. These questions relate to areas such as the safety of accounts of bank depositors, the safety of stockholder interests in banking organizations, and the ability of banking organization personnel to manage commercial ventures, to name a few.

Proponents of a strong banking organization role in an export trading company argue that active participation or control is necessary because many banking organizations have foreign branches, and therefore, have commercial contacts both domestically and abroad. A banking organization, it is argued, can serve as the catalyst that will bring together U.S. businesses and foreign markets. "Banking organizations" is defined by the bill to include state and national banks, as well as bank holding companies, bankers' banks, Edge Act Corporations and Agreement Corporations.

Our primary concern is for the protection of the depositors and shareholders in our commercial banks. Additionally, we are very concerned about the manner in which some of these financial institutions might operate in the future. The hearing record is virtually silent on these questions. In almost 1,000 pages of printed testimony there are but a few paragraphs which touch upon this area. Most of these comments questioned this new role of commercial banks. Treasury Assistant Secretary C. Fred Bergsten testified that:

> It is a long established principle in this country that banks should not be owners of commercial organizations. Giving banks an equity interest in the success of a commercial venture could bias their lending, trust, and other activities, and could require substantial policing to insure that such financial relationships are based solely on sound and equitable business considerations. The basic tenet of American law, that banking and banking related activities should be separate from other business practices, demonstrates the difficulty of transferring

to the United States the Japanese model, where bank-firm relationships are an integral part of the entire business and commercial structure.

Additionally, Paul Volcker, Chairman of the Federal Reserve Board, has expressed reservations about an expansion of the scope for banks to invest in commercial activities. The American Bankers Association has not appeared to testify on the bill and has no current position on the proposed legislation. Several officers of commercial banks whom we have contacted regarding this proposal have expressed a very cautious and "go-slow" approach to changing the powers of banking organizations.

In summary, we are concerned about the mounting merchandise trade deficit of the last few years. Much of this deficit results from declining domestic business productivity coupled with increases in the price and volume of energy imports. While we believe that export trading companies have an important role to play in increasing export opportunities, we do not believe they are a panacea for resolving our balance of trade problems. The model of the export trading company as it is known in Japan or Western Europe is not well understood by American businesses. It remains to be seen how it might adapt to U.S. business practices or how U.S. business practices might change to accommodate the model of foreign export trading companies. Until a better record is built as to how banking organizations might adjust to the new climate of not only financing, but directly participating in the management of commercial organizations, we believe it is wise to proceed very cautiously in promoting this new area of commercial activity.

JOHN TOWER.
ALAN CRANSTON.
JAKE GARN.

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